

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

MILBURN WATER DISTRICT FOR AN )  
ADJUSTMENT OF RATES PURSUANT )  
TO THE ALTERNATIVE PROCEDURE FOR ) CASE NO. 9300  
SMALL UTILITIES )

O R D E R

On March 18, 1985, Milburn Water District ("Milburn") filed an application with the Commission to increase its water rates pursuant to 807 KAR 5:076. This regulation permits utilities with 400 or fewer customers or \$200,000 or less gross annual revenues to use the alternative filing method to minimize the necessity for formal hearings, to reduce filing requirements and to shorten the time between the application and the Commission's final Order. This procedure minimizes rate case expenses to the utility and, therefore, results in lower rates to the ratepayers.

Milburn requested rates which would produce an annual increase of \$9,609 on a test year basis. In this Order, the Commission has allowed rates which will produce an annual increase of \$3,720.

There were no intervenors in this matter and no protests were entered. All information requested by the Commission has been filed.

### TEST PERIOD

Milburn has proposed and the Commission has accepted the 12-month period ending December 31, 1983, as the test period in this case.

### REVENUE AND EXPENSES

Milburn had a net operating income of \$1,767 for the test period. Milburn proposed numerous adjustments to test period revenues and expenses to reflect more current operating conditions which resulted in a net operating loss of \$10,738. The Commission has accepted Milburn's pro forma revenues and expenses with the following exceptions:

#### Operating Revenue

Milburn incurred operating revenue from metered water sales of \$20,432 for the test period. Milburn was permitted to increase the rates it could charge in Case No. 9210.<sup>1</sup> Therefore, the Commission has increased test period operating revenue from metered water sales by \$4,072, which results in an adjusted test period level of \$24,504.<sup>2</sup>

#### Purchased Water

Milburn proposed a pro forma purchased water expense of \$7,900 which reflected the increased rates from its supplier, the Fancy Farm Water District ("Fancy Farm"). In response to item

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<sup>1</sup> Purchased Water Adjustment of Milburn Water District, dated January 15, 1985.

<sup>2</sup> Original Application filed March 18, 1985, Revenue Table, Column Heading-PWA.

number 1c of the initial Commission request dated May 14, 1985, Milburn explained that this adjustment was calculated by using estimated water purchases of 9,875,000 gallons instead of the gallons actually billed by Fancy Farm of 8,280,000. Milburn went on to explain that estimated water purchases were used in this instance because the master meter which measured the water purchased from Fancy Farm was inoperable during the entire test period and was not replaced by Fancy Farm until May 1984. After the new master meter was installed Milburn discovered that the water loss was greater than what it had originally contemplated. Water loss rose from 5.85 percent during the test period to 24.5 percent in 1984, and the test period estimated water purchases were lower than what actually occurred.

The Commission recognizes that due to the faulty master meter Milburn's test period purchases are not an accurate reflection of what Milburn would normally purchase during a year. Therefore, the Commission is of the opinion that it would be fair, just and reasonable to adjust Milburn's test period water purchases to reflect a 15 percent water loss, which is the maximum allowed by this Commission for rate-making purposes. Thus, the Commission has determined the allowable gallons of purchased water for rate-making purposes to be 9,343,471 gallons,<sup>3</sup> which results in a reduction of \$425 from Milburn's proposed level of \$7,900 to arrive at the adjusted level of \$7,475.<sup>4</sup>

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<sup>3</sup> 7,941,950 gallons sold + 0.85 = 9,343,471.

<sup>4</sup> 9,343,471 gallons X 80¢ per 1,000 gallons = \$7,475.

### Depreciation Expense

Milburn's test period depreciation expense was \$4,132, which reflects depreciation on total plant using a composite rate of approximately 2.33 percent.<sup>5</sup> It is the Commission's practice to compute depreciation expense for rate-making purposes on the basis of original cost of the plant in service less contributions in aid of construction. The balance sheet filed by Milburn shows contributions in aid of construction at the end of the test period to be \$26,706. This amount is approximately 14.9 percent of the total cost of the utility plant in service. In determining a reasonable level of depreciation expense, the Commission has utilized the depreciation rate applied by Milburn and has excluded depreciation associated with contributed property. The adjusted depreciation expense for rate-making purposes is \$3,542,<sup>6</sup> a reduction of \$590.

### Maintenance Expenses

Milburn proposed the following pro form adjustments to test period maintenance expenses: an adjustment of \$1,200 for repairs to mains, an adjustment of \$375 for plant maintenance, and an adjustment of \$500 for pump maintenance. In response to item number 1f of the initial request and in the response to item number 4b of the second request dated August 7, 1985, Milburn

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<sup>5</sup>  $\$4,132 \div \$177,548 = 2.33\%$

<sup>6</sup>

Total Utility Plant	\$178,738
Less: Contributions in Aid of Construction	26,706
Non-Contributed Plant	<u>152,032</u>
Times: Composite Rate	2.33%
Depreciation Allowed for Rate-Making Purposes	<u>3,542</u>

stated that the proposed adjustments were based on Milburn's past experience, the past experience of other districts, discussions with both engineers and vendors, as well as the age of the system. It is the practice of this Commission to allow only known and measurable pro forma adjustments for rate-making purposes. It is the Commission's opinion that historic data, age of the system and discussion with engineers and/or vendors are not sufficient evidence to make these adjustments known or measurable since there are many variables that could attribute to the present and future need for maintenance, but none of these variables are readily identifiable and certainly not known or measurable. Therefore, the Commission has reduced test period operating expense by \$2,075.

#### Meter Maintenance

Milburn proposed a pro forma adjustment of \$1,857 to test period meter maintenance expense due to the planned checking, calibration and replacement of Milburn's meters. In the original application Milburn stated that the cost per meter for the checking and calibration would run approximately \$10 to \$15. In defense of the proposed adjustment Milburn claimed in the response to item number 1f of the initial request that the meters have been in use for approximately 16 years without any calibrative checks being performed and that the per meter cost of \$10 to \$15 was obtained via a phone conversation with Raleigh Bartlett, a certified meter checker. In response to the second request Milburn went on to add that it planned to have all of the old meters checked and recalibrated as soon as Milburn becomes financially

able and that Milburn was not exactly sure of the number of meters that would be checked per month. The Commission is aware that 807 KAR 5:066, Section 17, states that each utility shall test its water meters periodically; however, in this instance Milburn is not aware of when the plan will be actually implemented, the number of meters that will be checked per year and the exact per meter cost. The Commission is of the opinion that due to the number of uncertainties of this proposed adjustment it does not meet the criterion of being known or measurable. Therefore, the Commission has reduced Milburn's meter maintenance expense by the entire adjustment of \$1,857.

#### Wage Increases

Milburn proposed a pro forma meter reading and collection labor expense of \$6,000 and a related pro forma tax expense of \$200 for a combined increase of \$2,444 above test period operating expenses. Both adjustments were based on projected wage increases to Milburn's meter reader and bookkeeper. In response to item number 1e of the initial information request Milburn stated that the projected wage increases for both the meter reader and bookkeeper were based on hourly wage and time estimates and not on any specific test period data. Milburn revealed in response to item number 2a of the second request that the projected wage increases would be implemented after Milburn became financially able. This gives the Commission little certainty as to when or if the projected wage increases will be implemented. Since there is doubt as to when or if the projected wage increases will be implemented, the Commission is of the opinion that the projected wage increases

do not meet the criterion of being known or measurable. Thus, operating expenses have been reduced by \$2,444.

#### Rate Case Expense

Milburn proposed a pro forma accounting expense of \$1,500 and an advertising expense of \$75 for a combined increase of \$575 to test period operating expenses. In response to item number 1g of the initial request Milburn stated that the proposed increases were for the cost of filing Case No. 9210. In addition Milburn has indicated the cost of filing the present case is \$950. It is the opinion of the Commission that the filing of a rate case is normally a non-recurring expense and that it would be appropriate to amortize the cost of filing both cases over a 3-year period. Therefore, the Commission has reduced test period operating expenses by \$575 and increased test period amortization expense by \$508 for a net reduction of \$67.

#### Interest Expense

Milburn proposed a pro forma interest expense of \$4,238 to be included in its operating expenses. It is the practice of this Commission not to include interest expense in operating expenses, but to include it in the computation of net income as a below-the-line expense. Thus, test year operating expenses have been reduced and interest expense increased by the entire amount of interest expense of \$4,238.

Therefore, Milburn's test period operations have been adjusted as follows:

	<u>Milburn's Proposed Adjusted</u>	<u>Commission Adjustments</u>	<u>Commission Adjusted</u>
Operating Revenue	\$20,432	\$ 4,072	\$24,504
Operating Expense	\$31,170	<11,696>	19,474
Operating Income	<\$10,738>	\$15,768	\$ 5,030
Other Deductions			
Interest Expense	-0-	\$ 4,238	\$ 4,238
Net Income	<\$10,738>	\$11,530	\$ 792

#### REVENUE REQUIREMENTS

Milburn's annual debt service based on debt outstanding during the test period is \$7,292.<sup>7</sup> Milburn's adjusted net operating income of \$5,030 provides a debt service coverage ("DSC") of 0.69X. The Commission is of the opinion that this coverage is unfair, unjust and unreasonable. To achieve a DSC of 1.2X, which the Commission is of the opinion is the fair, just and reasonable coverage necessary for Milburn to pay its operating expenses and to meet the requirements of its lenders, Milburn would require a net operating income of \$8,750. Accordingly, the Commission has determined that additional revenue of \$3,720 is necessary to provide the 1.2X DSC which will ensure the financial stability of Milburn.

#### FINDINGS AND ORDERS

The Commission, after consideration of the application and evidence of record and being advised, is of the opinion and finds that:

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<sup>7</sup>	Bonds (5-year average principal 1986-1990)	\$3,400
	Interest (5-year average 1986-1990)	\$3,892
	Debt Service	\$7,292



1. The rates proposed by Milburn will produce revenues in excess of the revenues found reasonable herein and should be denied upon application of KRS 278.030.

2. The rates and charges in Appendix A are the fair, just and reasonable rates to be charged by Milburn in that they should produce gross revenues from Milburn's operations of \$28,224.


IT IS THEREFORE ORDERED that the rates proposed by Milburn be and they hereby are denied.

IT IS FURTHER ORDERED that the rates and charges in Appendix A be and they hereby are approved as the fair, just and reasonable rates and charges to be charged by Milburn for service rendered on and after the date of this Order.

IT IS FURTHER ORDERED that, within 30 days of the date of this Order, Milburn shall file revised tariff sheets setting out the rates and charges approved herein.

Done at Frankfort, Kentucky, this 11th day of October, 1985.

PUBLIC SERVICE COMMISSION

  
Chairman

  
Vice Chairman

  
Commissioner

ATTEST:

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Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 9300 DATED 10/11/85

The following rates and charges are prescribed for the customers of Milburn Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

<u>USAGE BLOCKS</u>	<u>RATES</u>
First 2,000 gallons	\$ 7.65 Minimum
Next 3,000 gallons	3.45 per 1,000 gallons
Next 5,000 gallons	2.75 per 1,000 gallons
Next 10,000 gallons	2.05 per 1,000 gallons
Over 20,000 gallons	1.65 per 1,000 gallons
Reconnection Fee	\$ 15.00
Tap Fee	430.00